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SMALL BUSINESS ADMINISTRATION

13 CFR Part 107

RIN 3245-AG66

Small Business Investment Company Program—Impact SBICs

AGENCY: U.S. Small Business Administration.

ACTION: Proposed rule; withdrawal.

SUMMARY: The Small Business Administration (SBA) is withdrawing its proposed rule published on February 3, 2016. In the proposed rule, SBA would have defined a new class of small business investment companies (SBICs) that would seek to generate positive and measurable social impact in addition to financial return. With the creation of this class of “Impact SBICs,” SBA sought to expand the pool of investment capital available primarily to underserved communities and innovative sectors as well as support the development of America’s growing impact investing industry. SBA is withdrawing the proposed rule because SBA has determined that the cost is not commensurate with the benefits.

DATES: SBA is withdrawing the proposed rule published on February 3, 2016 (81 FR 5666) as of [INSERT DATE OF PUBLICATION IN THE FEDERAL REGISTER].

FOR FURTHER INFORMATION CONTACT: Theresa Jamerson, Office of Investment and Innovation, (202) 205-7563, theresa.jamerson@sb.agov.

SUPPLEMENTARY INFORMATION:

I. Background Information

SBA's efforts in the impact investing space began on April 7, 2011 through a policy letter ("Impact Policy"), which was subsequently updated on September 26, 2012 and September 25, 2014. The purpose of the Impact Policy was to license small business investment companies ("SBICs") focused on generating both a positive and measurable social impact in addition to a financial return as "Impact SBICs." Licensed Impact SBICs were expected to provide at least 50% of their financings in "impact investments" as defined by the Impact Policy.

SBA published a Proposed Rule on February 3, 2016 (81 FR 5666) (the "Proposed Rule") to permanently define Impact SBICS and set forth regulations applicable to Impact SBICs with respect to licensing, leverage eligibility, fees, reporting and compliance requirements. The intent of the rule was to encourage qualified private equity fund managers with a focus on social impact to apply to the SBIC program. As part of the Proposed Rule, SBA would have provided the following three key benefits: (1) Impact SBIC applicants would have received a 60% discount on the licensing fee; (2) Impact SBICs would have received a 10% discount on the examination base fee; and (3) Impact SBICs could have simultaneously applied as an Early Stage SBIC not subject to the call and timing provisions identified under 13 CFR 107.300. Given these benefits, the proposed rule also imposed certain penalties if an Impact SBIC did not adhere to its impact strategy or the Impact SBIC rules.

II. Reason for Withdrawal

In determining whether to publish a final rule, SBA evaluated the results of the Impact Policy and the comments received in response to the Proposed Rule. In six years under the Impact Policy, few qualified funds applied to be licensed as Impact SBICs, and

SBA licensed only nine Impact SBICs. SBA believes that many of these SBICs would have applied to the SBIC program regardless of the existence of the Impact Policy. SBA determined that the cost of the Impact Policy was not commensurate with the benefits. On September 28, 2017, SBA provided notice to program stakeholders that SBA was cancelling the Impact Policy and would no longer accept applications to be licensed as an Impact SBIC on or after November 1, 2017.

Although SBA proposed licensing and examination fee discounts to provide further incentives for Impact SBICs as part of the Proposed Rule, SBA received one comment that all SBICs should be treated similarly in fee structure and no discounts should be offered. Three comments stated that the discounts are too small to provide an incentive sufficient to result in the formation of Impact SBICs, although two of these commenters stated that they nonetheless appreciated the discount.

Because Impact SBICs would have received certain benefits under the Proposed Rule, the Proposed Rule also identified penalties if an Impact SBIC failed to meet the requirements set forth in the rule, including failing to invest at least 50% of its financing dollars in impact investments and, for Impact SBICs using a Fund-Identified Impact Investment Strategy, failing to comply with certain specific measurement and reporting obligations. SBA received four comments stating that the Proposed Rule should not apply to Impact SBICs licensed prior to the effective date of any final rule, two comments stating that SBA should adjust the rules to reflect the policies under which the Impact SBICs were licensed, and one comment that suggested that existing Impact SBICs should be allowed the option to either complete their license under the relevant Impact Policy under which they were licensed or opt in to these new regulations. In reviewing

these comments, SBA determined that finalizing the rule would not likely result in an increase in the number of Impact SBICs in the program and would likely result in fewer Impact SBIC applications than SBA received under the Impact Policy. Although SBA licensed two Impact SBICs in each of FY 2015 and FY 2016, after publication of the proposed rule, SBA did not license any Impact SBICs in FY 2017.

SBA also considered costs in determining whether to withdraw the Proposed Rule. As noted in the Proposed Rule, due to the risk associated with this class of SBICs, and based on the amount of leverage SBA expected to allocate to the Impact SBIC program, the Proposed Rule was expected to increase the cost to all SBICs issuing SBA-guaranteed debentures by increasing the annual fee payable by all such SBICs by approximately 6.1 basis points. For an SBIC issuing \$100 million in SBA-guaranteed debentures, this would equate to \$61,000 per year. SBICs typically issue Debentures over a 4 to 6-year period (using multiple commitments) and begin paying back leverage as the fund harvests its investments. As a result, based on Debenture pools since 1992 that have been fully repaid, the average hold period is approximately 6 years, this would equate to \$366,000 in total additional fees for the SBIC. If the SBIC held the leverage outstanding for its full ten-year term, this would equate to \$610,000 for a single SBIC. Between FYs 2012 and 2017, SBA approved, on average, \$2.28 billion aggregate debenture commitments per year. If an additional 6.1 basis point charge were in effect, SBICs would incur over \$1.4 million per year in additional fees, or approximately \$8.3 million over the average 6-year average holding period for SBIC debentures. This is capital that SBICs could otherwise deploy to small businesses.

The withdrawal of the Proposed Rule has no effect on currently licensed Impact SBICs. Currently licensed Impact SBICs must continue to operate under the Impact Policy under which they were licensed (i.e., the Impact Policy issued in 2011, 2012 or 2014, as applicable). SBA will continue to follow SBA regulations and credit policies applicable to all SBICs with respect to approving leverage commitments and draws for Impact SBICs licensed with the intent of issuing SBA-guaranteed debentures. It should be noted that SBA allocated debentures for Impact SBICs in both FY 2018 and FY 2019 to accommodate existing Impact SBICs. SBA will determine the allocations of leverage for Impact SBICs for subsequent Fiscal Years after taking into account projected need by Impact SBICs in existence at that time.

Executive Order 13771

The withdrawal of the NPRM qualifies as a deregulatory action under Executive Order 13771. See OMB's Memorandum titled "Guidance Implementing Executive Order 13771, Titled 'Reducing Regulation and Controlling Regulatory Costs'" (April 5, 2017).

Accordingly, for the reasons stated in the preamble, the Proposed Rule published at 81 FR 5666 on February 3, 2016, is withdrawn.

Authority: 15 U.S.C. 634(b)(6).

Dated: May 12, 2018.

Linda E. McMahon,
Administrator.

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